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SUBJECT: NORWEGIAN ECONOMIC HIGHLIGHTS, NOVEMBER- DECEMBER 2005: STRONG 2005 ECONOMIC PERFORMANCE

Summary

¶1. (SBU) Summary of combined November-December monthly highlights:

* The past year was an exceptionally good one for the Norwegian economy: mainland real GDP grew by 3.9 percent; offshore petroleum investments reached a record high; the value of exports soared on account of rising crude oil prices; and the rich Government Petroleum Fund topped USD 200 billion.

* Norway's medium-term economic outlook is bright. The Central Bank expects low interest rates to contribute to sustained growth, though decelerating offshore oil and gas investments could lead to somewhat lower economic growth beyond 2006.

* Norway's Petroleum and Energy Minster confirmed that the 19th petroleum concession licensing round, which opens up additional Norwegian Sea and Barents Sea acreage, will go ahead as planned. Twenty-four firms submitted bids for acreage in these areas in November.

* Norway's 2005 offshore oil and gas investment is forecast to reach a record USD 13.7 billion.

* The new center-left government has indicated it will cease selling off shares of state-owned or controlled companies, including petroleum sector leaders Statoil and Norsk Hydro.

* Norsk Hydro announced that the company has made a significant find in Iran's Anaran field and will open discussions with Iranian authorities on developing the field.

* Little-known Norwegian petroleum independent DNO announced a potential major oil strike in a controversial project in Kurdistan and another in Yemen, sending the price of its stock soaring.

* American petroleum service firm National Oilwell Varco's $700 million investment in Norway was saved when the Renewal Ministry reversed a Competition Authority order that the company divest its local holdings due to their anti-competitive effect.

* U.S. petroleum investment in Norway took another leap when Texas-based Noble Corp. announced plans to purchase the Norwegian offshore drilling contractor Smedvig ASA, a $650 million deal.

* The word's longest (future) undersea natural gas pipeline, under construction between northern Norway and the UK, has reached the halfway point.

* Norway will impose stiff new taxes on light trucks next year that are expected to slash U.S. light truck imports by 90 percent.

* Russia, citing elevated levels of cadmium and other heavy metals in Norwegian salmon, announced it would ban Norwegian seafood imports effective January 1.

* Norway will require employers to pay a percentage of salaries into private pension funds next year, the first measure of its kind in Europe.

* The new center-left government raised taxes and

increased public spending in amendments to the 2006 budget, but signaled that it would not tap into the $200 billion petroleum fund for social spending. End Summary.

Norway's Strong 2005 Economic Performance

¶2. (U) Norway's economic performance over the past year has been impressive. Norway enjoyed one of the highest growth rates among OECD countries. Mainland GDP grew by 3.9 percent in real terms over the past year. Record offshore petroleum investments, forecast at around USD 14 billion for the year, and low interest rates contributed to the rapid growth. High petroleum investment levels were spurred by high capital outlays on Norway's two leading petroleum projects: the Snoehvit LNG development off Hammerfest and the Ormen Lange gas project.

¶3. (U) The Norwegian economy is still in a cyclical upturn. Unemployment remains low at an average of 4.5 percent for the year, though December saw an uptick to 4.8 percent. The Consumer Price Index edged up slightly in 2005 because of rising energy costs, but inflation remained very low at an average rate of only 1.5 percent for the year. Inexpensive imports from Asia and Central Europe continue to dampen inflationary pressures.

¶4. (U) With crude oil prices hovering near record highs for much of the year, Norwegian merchandise exports rose strongly, 19.5 percent by value. Norway's current account surplus swelled to USD 46 billion. Thanks largely to the growing current account surplus, Norway's Government Petroleum Fund (GPF), which is invested in overseas bonds and equities, rose to USD 209 billion in December. The GPF now roughly equals the United States' largest pension fund, the California Public Employees' Retirement System.

Economic Outlook: Slowing but Solid Growth
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¶5. (U) According to Central Bank of Norway economic projections, continued low interest rates should contribute to sustained growth over the coming year. A decline in offshore oil and gas investment from current record high levels, however, is expected, tending to dampen economic growth. The Central Bank projects that 2006 real mainland GDP growth will slow to 3.3 percent from this year's 3.9 percent. The Bank forecasts more moderate growth in medium term, in the 2.5 percent range in 2007-2008. To prevent the economy from "overheating," the Norwegian Central Bank raised key domestic interest rates (sight deposit rates) in November by 25 basis points to 2.25 percent, the second rate hike since August.

Record Norwegian Petroleum Investments

¶6. (U) Norway's 2005 offshore oil and gas investments are expected to top USD 13.7 billion, a new record. Norwegian Petroleum and Energy Minister Odd Roger Enoksen was quoted as saying that sharply higher crude oil prices are stimulating investment in Norway's offshore petroleum sector. The Snoehvit and Ormen Lange gas projects account for the bulk of the investment, but increased exploratory drilling is also

contributing. Enoksen said that Norway's goal is to maintain and build upon its world class extraction technology and its expertise in environmentally sound exploration and extraction techniques. Looking towards 2006, Snoehvit and Ormen Lange investment numbers are expected to decline, but total 2006 investment should remain high, at around USD 12 billion.

19th Oil/Gas Licensing Round Goes Forward
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¶7. (SBU) Norway's 19th petroleum concession licensing round, which will open additional Barents Sea acreage to exploration, is proceeding on schedule. Some observers had feared that Norway's new center-left government, which contains elements strongly opposed to Barents drilling, might sidetrack the round. Speaking on the margins of a

London petroleum conference, Petroleum Minister Enoksen confirmed that the new government would award the full 64 blocks in the Barents and Norwegian Seas, as planned by its predecessor. Enoksen noted that environmental protection and preservation of fishing grounds were important concerns, but should not suffer by going forward with the new licensing round.

¶8. (U) Twenty-four petroleum firms, including all U.S. companies active in Norway but ExxonMobil, submitted 19th round bids in November for new Barents Sea and Norwegian Sea licenses. The Petroleum Ministry expects to award the new production licenses towards the end of the first quarter of 2006. Minister of Petroleum Odd Roger Enoksen, commenting on the bid submissions, said he was "very pleased with the interest the companies are demonstrating for new exploration opportunities in the Barents Sea and the Norwegian Sea . . . it is clear that the competition for acreage is increasing also in frontier parts of the shelf."

Privatization Frozen

¶9. (SBU) Petroleum Minister Enoksen confirmed reports that the new center-left government would not sell additional shares in state-owned Statoil and state-controlled Norsk Hydro, Norway's two largest oil companies. The government owns 70.9 percent of Statoil and 43.8 percent of Norsk Hydro. Enoksen's announcement is consistent with the new government's stance that further privatization of Norway's major state-controlled firms should be halted. Some members of the new government have even advocated that the state reacquire shares it had previously divested.

Hydro Strikes it Big in Iran

¶10. (U) Norsk Hydro announced in early December that the it may have struck significant oil in Iran's Anaran field, where it has been exploring in partnership with Russia's Lukoil. Hydro says the discovery could possibly be the largest in 20 years. Hydro owns 75 percent of the field while Russian Lukoil owns the rest. The company has delivered its Development Plan to Iranian authorities and will seek to conclude a development agreement. A Hydro executive said Anaran "could prove to be one of the most important finds in recent years," yielding as much as 200,000 barrels per day.

¶11. (SBU) Hydro executives say the company is in Iran for the long haul. Spokesman Tor Steinum said Hydro intended to initiate talks with Iranian officials regarding long-term development projects. Hydro CEO Eivind Reiten also emphasized in a public statement that Norsk Hydro would pursue exploration and development projects in Iran, notably at Anaran and in the Khorramabad exploration block. The investments naturally raise Iran-Libya Sanctions Act concerns for the United States.

DNO Strikes it Big in Iraq, Yemen, and Oslo Bourse

¶12. (U) The small, independent Norwegian oil company Det Norske Oljeselskap (DNO) announced in December that it struck oil with its first well in the Kurdish region of Iraq. DNO has not estimated the size of the find, saying that more testing is needed, but believes the reservoir could be very thick.

¶13. (SBU) DNO entered into a controversial exploration agreement with the regional Kurdish government, which central authorities in Baghdad may or may not have blessed, in 2004. The new Iraqi constitution is reportedly murky on the authority granted to regional authorities to enter into such arrangements. DNO Managing Director Helge Eide told the press that he was confident that the deal was consistent with the new Iraqi constitution.

¶14. (U) Following on the heels of the Iran news, DNO announced in late December that it also may have hit oil in Yemen's Nabrajah field. DNO owns 56.7 percent of the field, Oil Search (Australia) owns 28.3 percent, and the Yemen Company completes the partnership with 15 percent. The announcements

have propelled the obscure company to the top of the most traded list on the Oslo stock exchange and have doubled the value of the stock in the last month.

Norway Rescinds Divestiture Order to U.S. Oil Firm
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¶15. (SBU) In November the Ministry of Renewal overturned a National Competition Authority (NCA) order to National Oilwell Varco (NOV), a leading U.S. petroleum service firm, to divest its assets in Norway. The NCA issued the divestiture order, which jeopardized NOV's $700 million local investment, because it found that a global merger between National Oilwell and Varco had anticompetitive effects on the Norwegian Continental Shelf. The Renewal Ministry ruled, however, that the NCA had defined the relevant market too narrowly in focusing only on the Shelf and that the market for drilling equipment was, in fact, global. Embassy staff and NOV executives cooperated closely in campaigning for a reversal of the divestiture order.

Texas' Noble Corp to Buy 40 Percent of Smedvig
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¶16. (U) U.S. investment in the Norwegian petroleum services sector received another boost in December when Texas-based Noble Corporation, one of the world's largest offshore drilling contractors, announced its intent to acquire 40 percent of Smedvig ASA, a leading Norwegian offshore drilling

firm. The deal is reportedly worth about USD 650 million. Smedvig has operations in nine countries and a workforce of 3,750 employees, more than half outside Norway.

Ormen Lange Gas Pipeline Halfway to England
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¶17. (U) Norsk Hydro's $10 billion Ormen Lange project reached a milestone in November when the project's subsea gas pipeline, which when completed will be the world's longest, reached the half-way mark. The 1,200 kilometer pipeline will run from Nyhamna in northwest Norway to Easington in the UK. The pipeline will eventually move some 70 million cubic meters of gas annually from the Ormen Lange field to the UK, providing up to 20 percent of Britain's gas supplies.

Hefty Taxes Likely to Kill U.S. Light Truck Imports
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¶18. (SBU) In November, Norway's new left-of-center government enacted a hefty new tax on light trucks (3.5 to 7.5 tons), effective January 1, 2006. The tax will increase retail prices by 50 to 90 percent and severely curtail demand for the vehicles, many originating in the U.S. American automobile importers protested the tax and its quick implementation deadline, which did not allow sufficient time to land vehicles currently in ocean transit in Norway. Faced with significant losses on more than 100 trucks ordered before the announcement, but still in transit, importers lobbied the Finance Ministry for an extension.

¶19. (SBU) The Embassy successfully made the importers' extension case to the Finance Ministry, which agreed just ten days before the deadline to postpone the implementation date to April 1. The Embassy and U.S. truck importers, who expect the tax to slash sales from more than 1,000 in 2005 to 100 or so in 2006, will continue to work for its rescission.

Russia, Citing Metal Levels, Bans Norwegian Salmon
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¶20. (U) Norway risks losing the Russian market, its largest, for fresh and frozen fish if a resolution is not found to a dispute over levels of cadmium and other metals in Norwegian fish. Russian veterinary inspectors claim to have found unusually high heavy metal levels in Norwegian farmed salmon and fish feed. Russian agricultural officials announced December 20 that Russia would cease buying not only farmed salmon, but all Norwegian seafood as of January 1, 2006. Russia is the largest importer of Norwegian fish products, purchasing over $200 million worth of Norwegian

salmon alone in 2005.

¶21. (U) Singapore, a large importer of Norwegian salmon, subsequently conducted its own inspections and concluded that Norwegian farmed salmon contained no heavy metals and was safe for consumption. Japan also conducted tests that backed up Singapore's results.

¶22. (SBU) Fisheries Ministry officials plan to discuss the dispute with Russian authorities on January 12 in Moscow. Most observers in Oslo believe the measure is politically motivated, probably in retaliation for Norway's recent

seizures of several Russian fishing trawlers fishing illegally in its waters. One Norwegian official wondered whether the ban would extend to Norwegian fish caught by poaching Russian trawlers.

New Mandatory Pension Payments to Private Funds

¶23. (U) In an effort to mitigate the financial pressure Norway's aging population is placing on its generous pensions system, the Parliament enacted a bill on December 20 that requires employers to pay two percent of an employee's salary into private pension funds. The measure, which takes effect July 1, 2006, is the first of its kind in Europe. Annual contributions are forecast at between $440-$590 million. Private asset management companies, banks and insurance companies are lining up to break into this new market.

New Government Raises Taxes and Spending

¶24. (SBU) The new center-left government unveiled several "socialist-style" measures in its November amendments to the 2006 budget adopted by the preceding center-right government in October. While the revised budget still calls for a surplus of USD 38 billion, the new government increased spending by USD 1.2 billion and raised taxes by USD 1.9 billion. Finance Minster Kristin Halvorsen, leader of the Socialist Left Party, justified higher tax rates on medium to high incomes and higher excise taxes as necessary to finance more public spending on local government. In a more fiscally conservative move, Halvorsen indicated that the new government would not tap into Norway's $200 billion petroleum fund for social spending, as many have urged.

----- Key Economic Indicators for Norway [a] ------

- GDP Growth:

Category	Volume Growth [Pct] 2004	2005	2006	2007	2008
Private Consumption	4.4	3.8	3.8	2.5	2.3
Public Consumption	2.3	1.8	2.0	1.8	3.0
Oil and Gas Investm.	12.3	20.0	2.5	[2.5]	[5.0]
Mainland Invest.	6.1	7.8	6.0	3.3	2.5
Exports	0.9	3.5	2.7	3.5	3.3
Imports	9.1	7.3	4.5	2.3	1.8
Mainland GDP	3.5	3.9	3.3	2.5	2.5
Total GDP	2.9	2.5	2.8	2.3	2.3
- Unempl. Rate[Pct][b]	4.5	4.5	4.0	4.0	4.0
- Inflation [Pct][c]	0.4	1.5	2.0	2.0	2.5
- Wage Growth [Pct]	3.5	3.5	4.3	4.5	4.5
- Int.Rate [M.Mkt;Pct]	2.0	2.1	2.2	2.2	2.4
Current Account Balance [NOK Bill]	228	319	416	366	356
- Crude Oil Price [d]	257	356	368	311	312
- Foreign Exch. Rate [NOK/USD]	6.7	6.4			
- U.S. Exports to Norway [USD Bill][e]	1.60	1.83			
- U.S. Imports From Norway [USD Bill][e]	6.51	7.01			

Notes: [a] Sources: The Ministry of Finance; The

Norwegian Central Bureau of Statistics [CBS]; The Central Bank; [b] Surveyed unemployment; [c] Consumer price inflation; [d] Brent Crude Spot Price: NOK/Barrel; [e] Source: USDOC

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